Real Estate OUTLOOK

September 1991

The sustainability of the budding recovery has been called into question by the mixed signals from the monthly economic indicators. August's decline in personal income and the steady erosion of consumer confidence hint at a return to recession, while the 11% gain in durable goods orders, a string of increases in industrial production and lower inflation suggest a healthy recovery. NAR projects that the economy will muddle through the remainder of the year before staging a robust recovery beginning early next year. *Page 2*

Housing starts continued their ascent in July, increasing 3.7% to an annual rate of 1.07 million units. July's figure is the highest since November of 1990, but starts remain 7.4% below the figure recorded one year ago. Building activity in the South accounted for much of the increase in July. There, starts increased 15.2% to 448,000 units. *Page 4*

After increasing for five consecutive months, the rate of existing home sales reversed its course in July. Sales dropped 6.7% from June's resale rate of 3.59 million units. Now that some of the demand that had been pent-up since last fall has been filled, existing home sales are expected to return to a more sustainable course of growth. *Page 6*

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Fear Strikes Out (Looking)

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The power of ideas. Christ and Mohammed transformed the world with them. Jefferson created the most powerful political movement in history with his. And two centuries ago, Adam Smith put together a collection of ideas that last month caused hell to freeze over. For the first time in their thousand year history, the peoples of the Soviet Union were told by their leaders to do something and they refused, because the power of the ideas of free markets and democracy were stronger than their fears.

In retrospect, it was no contest: a badly planned coup by the gray-haired and gray-faced leaders of a government where mismanagement is a culture. It was Boris Yeltsin against Boris Badanov. But when the popguns of August went down, they were defeated by a people who had seen how freedom works and were not going back.

It's easy to analogize the current state of the Soviet Union to that of the American colonies in 1781. Here are a number of newly independent states, freed from the tyranny of statist oppression, ready to burst forth as capitalist democracies.

But it's far from the same. Unlike the American colonies, Russia and the Baltic States and the Ukraine have no traditions of either democracy or capitalism on which to build. Rather, they are inspired by ideas and now need to invent the institutions and processes that will make those ideas real in their lives. Their reality is that of the Third World.

Right now, the Soviet economy is bankrupt and facing a potential winter disaster. So the calls for aid from the developed world followed right on the heels of the departing tanks. The West should respond immediately, despite the threat (so pointedly noted by the Wall Street Journal) that aid now would only prop up Gorbachev without forcing him to commit to reform.

But, remembering the difference between giving fish and teaching how to fish, the longer term challenge is to provide the technical assistance that will enable the creation of free market institutions and systems. This builds a capacity to absorb the American investment now so hotly debated, and ultimately will feed back into the U.S. economy in the form of strong demand for American goods.

Clearly, the whole thing can turn around in a day, and the hardliners can make yet another *putsch*. But it's not likely. The drive for reform and free markets is too strong, and even though they will come slowly and grudgingly, they will come. The great issue of whether the events of August will speed reform in the Soviet Union seems to have been decided in the affirmative.

Interestingly, few are raising an equally telling issue: Will the events of August speed reforms in the United States? We have lived for centuries guided by the ideas that are now lighting flames in the East, just as they have inspired other nations. Yet, we seem to have forgotten a great many of them. And when we forget the roots from which we spring, we manage to create the Charles Keatings and the BCCIs of the world.

Capitalism promises great rewards, but also carries great risks. Our economy was shaped by a process of success and failure that are equal sides of the capitalist coin. Yet, now we talk about banks that are "too big to fail" and social insurance systems that protect all people and businesses against all mistakes.

Capitalism requires markets in which the price mechanism is free to operate and in which entry and exit are relatively easy. Yet, our system now seems to regulate everything from automobile components to the distance between door frame and window sill in a new house.

Capitalism requires a continual infusion of new resources and ideas through the process of investment, so that the surplus it creates can be used to build future earnings. Yet, we now live in an economy which in its public policies discourages all forms of investment, and especially its most productive, that in real estate.

Capitalism requires a political system in which power flows to wealth (and this may be the hardest of all lessons for the Soviets to learn), not the reverse. Yet, in our government of constant campaigning, power is independent of wealth and, in a highly regulated society, seems to attract it.

Cataclysmic events cause humans to take stock, so funerals and weddings are usually the occasion for much soul searching. The disintegration of the Soviet empire and the coming (we hope) democratic future should likewise cause us to examine our own society, and the degree to which it has strayed from the ideal of free market democracy.

If the movement to a Soviet market economy is to have a motto, there are few better than the words of Albert Einstein:

> *Everything that is really great and inspiring is created by the individual who can labor in freedom.*

All the ideas that matter -- individual, labor, freedom -- are there. Every now and again we need to remember just how powerful they can be.

Outlook for the Economy

The sustainability of the budding recovery has been called into question by recent economic reports, some of which suggest that the recession may still be lingering. The mixed signals from the monthly economic indicators highlight the economy's current transitional nature, but just where we're headed remains unclear. August's decline in personal income and the steady erosion of consumer confidence suggest a return to recession, while the 11% gain in durable goods orders, a string of increases in industrial production and lower inflation suggest a normal, healthy recovery. Meanwhile, the anemic employment gains indicate that the recovery will remained hobbled.

While noting the possibility of another recessionary dip in production, NAR projects that the economy will muddle through the remainder of the year before staging a robust recovery beginning early next year. After nine months of decline, output in the third quarter is projected to expand at a 2.9% annual rate, the fastest rate since early 1989. The composition of that growth -- powered by inventory rebuilding, not increasing demand -- means that the recovery is relying on a temporary boost for its health. Consequently, growth is expected to slide down a notch to 2.3% in the year's final quarter. The year is expected to post a 0.3% decline, and a 2.5% rebound is projected for 1992.

Missing in Action: Persistent Demand Gains

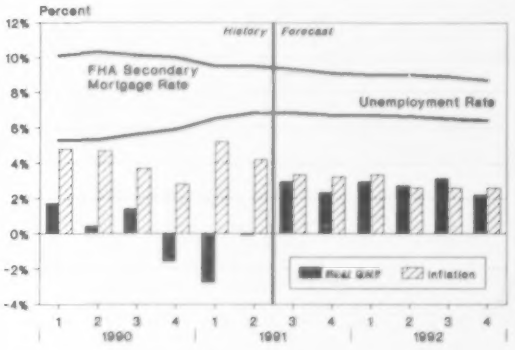
Feeling relief over the end of seven months of Persian Gulf tension, consumers jump-started the economy last spring. Sales of both new and existing homes rose sharply, and spending on consumer goods bounced back. The growth in spending was answered largely by a liquidation of inventories, while businesses, concerned about rising debt levels and credit availability, waited to see if the renewed strength in spending would last before stepping up production. Now, it appears, just as businesses are gearing up again, consumer enthusiasm is on the wane.

Consequently, growth in the third quarter is expected to come from a source that won't provide much long-term relief: replenishing drawn-down inventories. All of the economy's production -- its GNP -- can be broken down into two parts: that which is sold (final demand) and that which is stored and sold later (changes in inventories). The bulk of the economy's growth in the third quarter will come from the additions to inventories, accounting for 2.4 percentage points of the total 2.9% increase. The remaining 0.5 percentage points will be demand's meager contribution.

The implication is this: If demand remains sluggish, then once the stocks are replenished, production schedules may again be pared down. For the recovery to be sustained beyond year-end, other sectors of the economy will need to step forward and provide the necessary stimulus. Government spending is constrained by deficits on the federal, state, and local levels. Exports will continue to provide some help, but that will likely diminish in the face of the dollar's recent appreciation. Businesses are projected to boost equipment spending, but this accounts for less than 10% of the economy's total production.

As usual, then, it will be up to the consumer. Because consumption spending accounts for two-thirds of the total

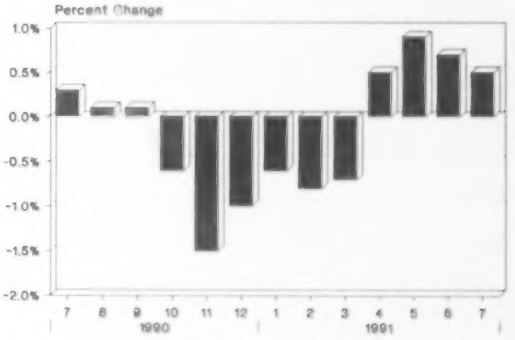
The Economic Outlook



Sources: BEA, BLS, FHLMC, NAR forecast

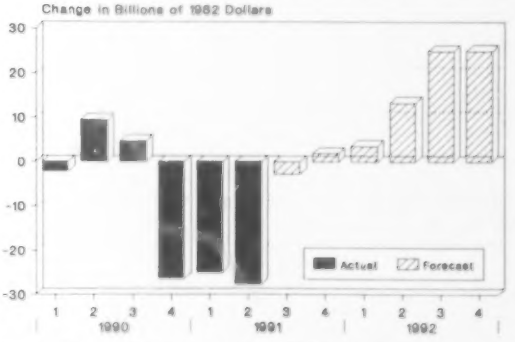
Industrial Production Recovers

But Slack Demand May Lead to Smaller Increases



Source: Federal Reserve Board

Inventory Liquidation in First Half Sets Stage for Growth



Source: Bureau of Economic Analysis; NAR forecast

GNP, the economy usually steps to the beat of the consumer's drum, and recently the rhythm has been fading. The consumer confidence index has fallen in four of the past five months, an omen of lethargic consumption growth in the months ahead. The fundamentals behind household spending -- income and employment -- have shown only weak growth in the past few months. It's for these reasons that we believe the recovery will remain tepid.

Job Gains Point to Subdued Recovery

The chart at right shows how the character of the monthly change in employment has improved since April. The declines recorded in June and July were very modest, especially relative to the losses racked up between last October and April. While May's and August's figures were up, they fell short of the average gain recorded during the last economic expansion.

Manufacturing has been hit hard, and not just by the recession. Production had been on the skids for more than a year before the official start of the recession in July 1990. In fact, manufacturing employment has grown in only five of the 32 months since the beginning of 1989. Three of those five months have come since May, signaling that a turnaround is finally in the works. In August, 42,000 workers returned to manufacturing payrolls.

Continued Good News on the Inflation Front

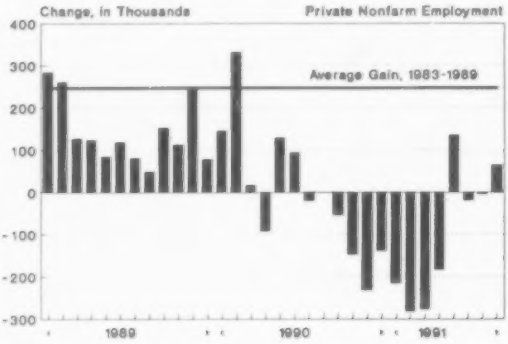
After sharp increases related to last fall's rising energy prices, the inflation rate has continued to moderate. The unwinding of oil prices and the weak economy have limited the increase in consumer prices to just a 2.7% annual rate since last December. The core rate of consumer inflation, defined as the total Consumer Price Index less its volatile energy and food components, rose 4.8% in the twelve months ending in July. This is a significant decrease from the 5.6% rate measured over the twelve months ending last February. As the chart shows, the monthly reports on producer prices have been positive as well, with two declines registered in the past two months.

One hurdle to the recovery has been lowered significantly. Long-term interest rates broke in mid-August, with rates on conventional 30-year mortgages falling almost a third of a point during the month. As the chart shows, rates drifted up during the spring and early summer, but tumbled in August with the growing realization that the recovery was sluggish and inflation was under control. Still, given the recent inflation performance, long-term interest rates remain high. This apparently reflects the fear that the Federal Reserve, in order to revive the recovery, may pump up the economy too fast and introduce additional inflation.

The Fed, for its part, is at a critical juncture. It is well aware that the most serious errors committed by previous Fed boards have come after the economy has turned the corner but before that turn is evident. Hindsight shows that too much stimulus was provided during this period, resulting in extra inflation. Adding to the dilemma are today's banking problems, such as the credit crunch, which make the usual monetary compasses less reliable. The forecast assumes a further easing in the next month, as the Fed cuts its discount rate a half-point to 5.0%.

Employment On The Mend

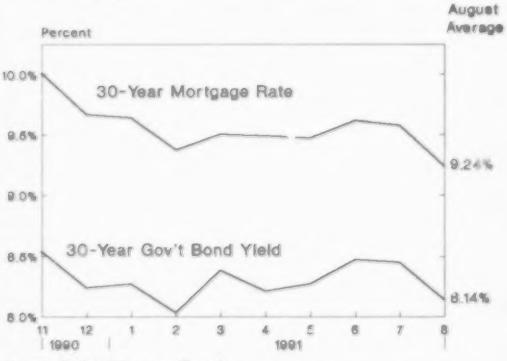
Steep Declines Over, But Recent Gains Weak



Source: Bureau of Labor Statistics

Long-Term Rates Fall in August

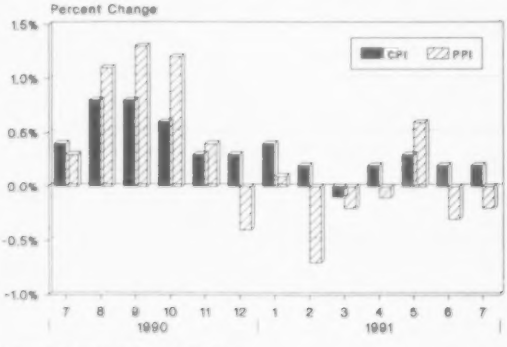
Mortgage Rates at Their Lowest Since February



Source: Federal Reserve Board

Inflation Winding Down

Recent Reports May Give Fed Room To Ease Further



Source: Bureau of Labor Statistics

Housing Starts

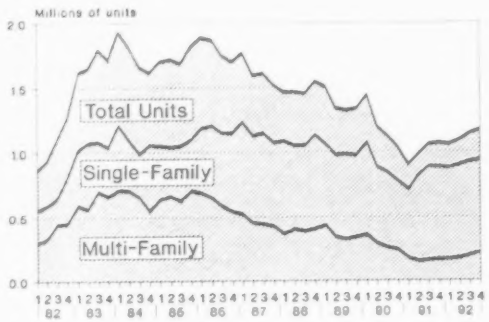
National Data

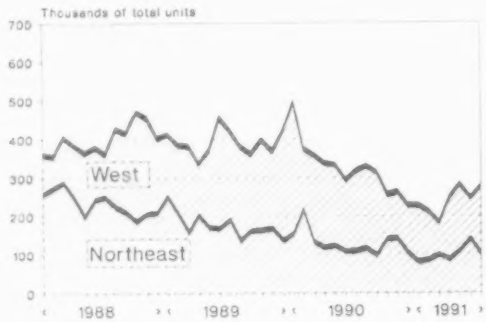
	Total	SF	MF:2-4	MF:5+
Jul 1990	1,155	876	31	248
Feb 1991	992	788	37	167
Mar 1991	907	742	28	137
Apr 1991	977	801	32	144
May 1991	983	831	36	116
Jun 1991	1,032	862	26	144
Jul 1991	***1,070***	***894***	***48***	***128***
Annual Averages:				
1989	1,381	1,005	56	320
1990	1,203	901	37	265
Percent Changes in July 1991 since:				
Jul 1990	-7.4	2.1	54.8	-48.4
Jun 1991	3.7	3.7	84.6	-11.1

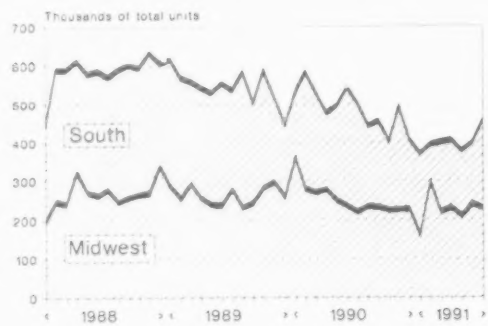
Regional Data

	Northeast	Midwest	South	West
Jul 1990	115	226	492	322
Feb 1991	91	301	384	216
Mar 1991	104	226	390	187
Apr 1991	93	236	395	253
May 1991	114	216	367	286
Jun 1991	145	246	389	252
Jul 1991	***106***	***235***	***448***	***281***
Annual Averages:				
1989	181	269	535	397
1990	135	259	478	330
Percent Changes in July 1991 since:				
Jul 1990	-7.8	4.0	-8.9	-12.7
Jun 1991	-26.9	-4.5	15.2	11.5

Levels are seasonally adjusted annual rates, in thousands.
Source: Bureau of the Census, Construction Reports, Series C25







Housing starts continued their ascent in July, increasing 3.7% to an annual rate of 1.07 million units. July's figure is the highest since November of 1990, but starts remain 7.4% below the figure recorded one year ago.

Continued gains in housing starts are evidence of the growing recovery in the residential construction market. Starts of single-family homes increased 3.7% to an annual rate of 894,000 units. Starts of multifamily homes recorded an overall increase of 3.5% in July, but the performance of the individual categories of multifamily homes was mixed. The construction of homes with 2 to 4 units surged 84.6% to 48,000 units, while the construction of homes with 5 or more units declined 11.1% to 128,000 units.

Building activity in the South accounted for much of the increase in July. After rising 6.0% in June, starts increased another 15.2% in July, bringing the annual rate to 448,000 units. Starts also advanced in the West, with an increase of 11.5% to 281,000 units. After an impressive performance during the second quarter, starts in the Northeast decreased a disappointing 26.9% in July. A decline of 4.5% in the Midwest brought the rate of starts down to 235,000 units.

Housing starts should average 1.08 million units during the second half of this year. Falling mortgage rates accompanied by a looser lending environment will fuel housing construction in 1992. Total starts will post a healthy 11.0% gain over 1991, with multifamily starts leading the rally. The construction of multifamily homes will increase 15.1% in 1992, while single-family starts are expected to increase 10.1%.

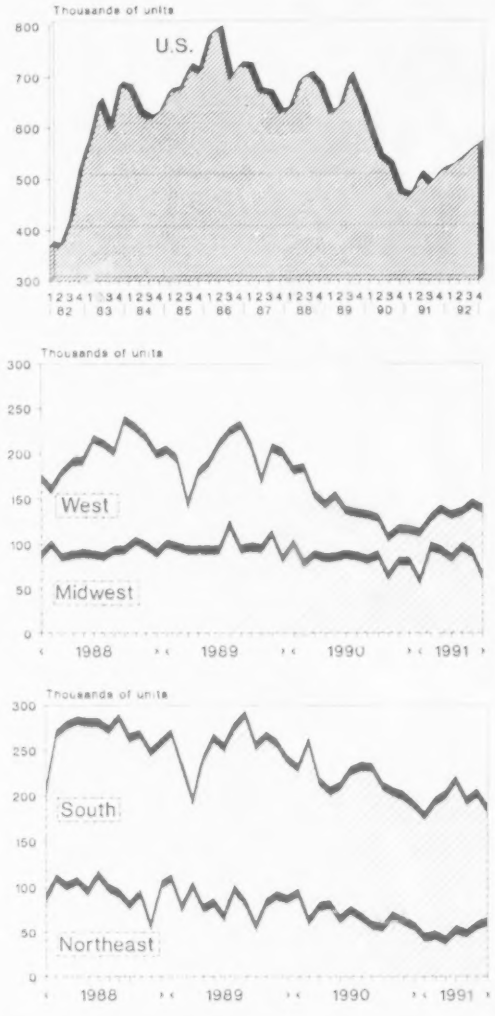
National Data

		Mo. Ago % Chg.	Yr. Ago % Chg.
Jul 1990	541	-1.5	-27.0
Aug 1990	525	-3.0	-27.0
Sep 1990	504	-4.0	-21.0
Oct 1990	465	-7.7	-26.9
Nov 1990	480	3.2	-30.1
Dec 1990	464	-3.3	-26.7
Jan 1991	414	-10.8	-34.0
Feb 1991	488	17.9	-19.5
Mar 1991	495	1.4	-11.4
Apr 1991	506	2.2	-5.2
May 1991	496	-2.0	-7.1
Jun 1991	516	4.0	-6.0
Jul 1991	***472***	***-8.5***	***-12.8***
Annual Averages:			
1989	654		-3.3
1990	534		-18.3

Regional Data

	Northeast	Midwest	South	West
Jul 1990	72	92	237	140
Feb 1991	52	102	199	134
Mar 1991	46	99	206	144
Apr 1991	58	90	222	137
May 1991	54	102	199	141
Jun 1991	63	95	208	150
Jul 1991	***67***	***69***	***191***	***144***
Annual Averages:				
1989	90	103	258	202
1990	75	90	222	147
Percent Changes in July1991 since:				
Jul 1990	-6.9	-25.0	-19.4	2.9
Jun 1991	6.3	-27.4	-8.2	-4.0

Levels are seasonally adjusted annual rates, in thousands.
Source: Bureau of the Census, Construction Reports, Series C25



New home sales fell below the half-million mark in July. The annual rate of sales stood at 472,000 units, which is 8.5% below June's rate and the lowest level since January of 1991. The upward drift in mortgage rates in the spring and the end of the release of the demand that had been pent-up since last fall are likely the causes of July's decline in sales.

Of the four Census reporting regions, the Northeast was the only region to record a gain in July. After increasing nearly 17.0% in June, sales climbed another 6.3% in July to 67,000 units. Although this figure remains 6.9% below the sales rate of one year ago, the latest monthly increases indicate that recovery is proceeding in the region that was hardest hit by the recession.

Of the remaining three regions, the Midwest encountered the greatest losses in July, decreasing 27.4% to 69,000 units. In the South, sales dropped 8.2% to 191,00 units. Sales also faltered in the West, falling 4.0% to 144,000 units. Even with this decline, sales remain 2.9% above the figure one year ago.

According to the NAR forecast, the rate of new home sales will average 499,000 units during the latter half of 1991. During the first half of 1992, the pace of sales is expected to accelerate, averaging 527,000 units. Additional gains are expected for the remainder of 1992, and for the entire year sales are expected to post a 10.1% gain over 1991.

Lower mortgage rates will continue to stimulate sales into 1993. Overall, the rate of new home sales is forecast to increase a robust 9.4% to an annual rate of 593,000 units in 1993.

Existing Home Sales

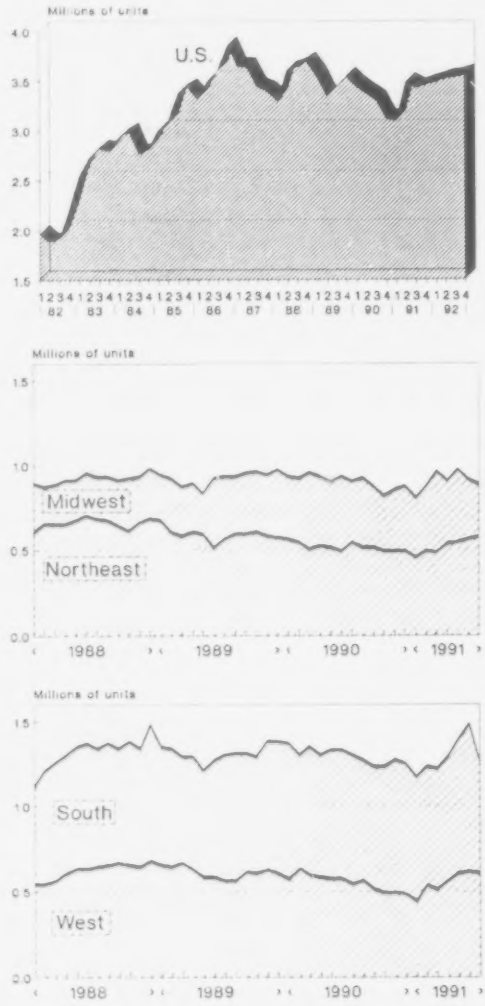
National Data

		Mo. Ago % Chg.	Yr. Ago % Chg.
Jul 1990	3,320	-1.5	-1.8
Aug 1990	3,410	2.7	-1.8
Sep 1990	3,160	-7.3	-0.9
Oct 1990	3,070	-2.8	-10.0
Nov 1990	3,150	2.6	-12.0
Dec 1990	3,130	-0.6	-11.5
Jan 1991	2,900	-7.3	-12.1
Feb 1991	3,160	9.0	-16.4
Mar 1991	3,220	1.9	-7.6
Apr 1991	3,310	2.8	-6.4
May 1991	3,540	6.9	-1.8
Jun 1991	3,590	1.4	5.7
Jul 1991	***3,350***	***-6.7***	***6.5***
Annual Averages:			
1989	3,440		-4.3
1990	3,296		-4.2

Regional Data

	Northeast	Midwest	South	West
Jul 1990	550	910	1,310	550
Feb 1991	500	880	1,240	540
Mar 1991	490	970	1,230	520
Apr 1991	540	910	1,300	570
May 1991	550	980	1,400	610
Jun 1991	570	920	1,490	620
Jul 1991	***580***	***890***	***1,270***	***610***
Annual Averages:				
1989	589	919	1,307	610
1990	522	892	1,325	557
Percent changes in July 1991 since:				
Jul 1990	5.5	-2.2	-3.1	10.9
Jun 1991	1.8	-3.3	-14.8	-1.6

Levels are seasonally adjusted annual rates, in thousands.
Source: National Association of Realtors, 'Home Sales'



After increasing for five consecutive months, the rate of existing home sales reversed its course in July. The resale rate dropped 6.7% to 3.35 million units. Despite the decline, July's figure remains 6.5% above the rate of one year ago. The surge of activity that occurred during the last few months reflected renewed consumer optimism at the close of the Gulf War and a desire to take advantage of low mortgage rates. Now that some of the pent-up demand has been filled, the market is expected to return to a more sustainable course of growth.

Of the four Census reporting regions, the Northeast was the only region to post a gain in resales during July. There, sales increased 1.8% to an annual rate of 580,000 units. Of the remaining three regions, the South saw the biggest decline in July, as sales decreased 14.8% from June's rate of 1.5 million units. Sales also edged down in the Midwestern and Western regions. The Midwest experienced a 3.3% decline in the sales rate to 890,000 units, while the West saw sales drop off 1.6% to 610,000 units.

By year end the resale rate is expected to stand at 3.46 million units. As a result of the robust activity during the spring of this year, sales should average 3.36 million units in 1991, which translates into a 2.1% gain over 1990's rate.

The momentum established in 1991 will position the resale market for stable growth in 1992 and 1993. In 1992, sales are projected to increase 4.7% to an annual rate of 3.52 million units. In 1993, the rate of existing home sales will continue to increase, but at the slower pace of 2.8%.

National Data

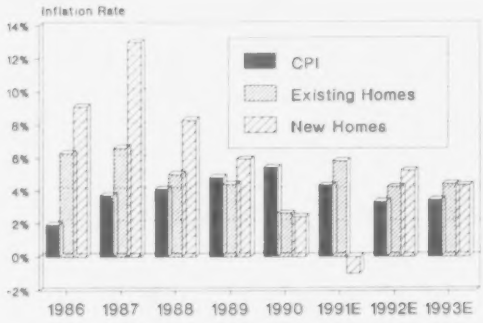
	Median		Average	
	Existing	New	Existing	New
Jul 1990	98,100	118,700	121,100	149,800
Feb 1991	94,000	119,900	119,700	147,800
Mar 1991	98,200	122,500	125,200	156,400
Apr 1991	100,300	121,000	128,900	150,800
May 1991	101,100	118,000	130,600	147,400
Jun 1991	102,000	121,100	130,500	147,000
Jul 1991	***103,000***	***120,200***	***131,600***	***151,000***
Annual Averages:				
1989	93,100	120,400	118,100	148,300
1990	95,500	122,300	118,600	149,100
Percent changes in July 1991 since:				
Jul 1990	5.0	1.3	8.7	0.8
Jun 1991	1.0	-0.7	0.8	2.7

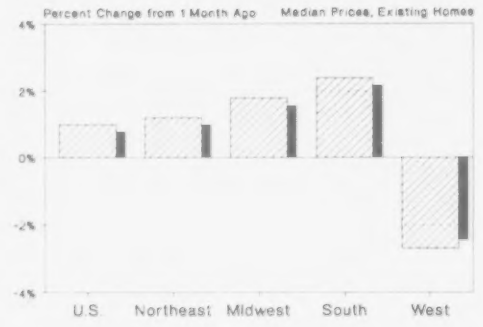
Regional Data

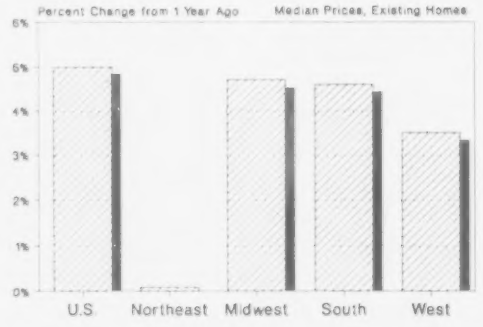
Median Prices for Existing Single-Family Homes

	Northeast	Midwest	South	West
Jul 1990	143,300	76,100	88,800	139,700
Feb 1991	137,200	76,400	83,200	137,100
Mar 1991	142,700	78,200	87,300	147,300
Apr 1991	144,800	77,900	88,000	151,000
May 1991	144,900	77,500	88,900	152,100
Jun 1991	141,800	78,300	90,700	148,600
Jul 1991	***143,500***	***79,700***	***92,900***	***144,600***
Annual Averages:				
1989	145,200	71,300	84,500	139,900
1990	141,200	74,000	85,900	139,600
Percent changes in July 1991 since:				
Jul 1990	0.1	4.7	4.6	3.5
Jun 1991	1.2	1.8	2.4	-2.7

Levels are shown in dollars.
Source: National Association of Realtors, 'Home Sales'







Since March of 1991, the median price of existing single-family homes appreciated 9.6%, or $9,000. Home sellers were under less pressure to lower prices this spring, as the close of the Persian Gulf war and lower mortgage rates rekindled the demand for homes.

Meanwhile, in the market for new homes, the median price partially reversed June's 2.6% increase with a 0.7% decrease in July. It now stands at $120,200, up 1.3% from the median price one year ago.

The average price of existing homes increased 0.8% in July to $131,600. When compared with July of 1990, the average price has risen 8.7%.

On a regional basis, the West was the only region which did not record an increase in the median price of existing homes in July. There, the median price dropped 2.7% from June's figure of $148,600. Each of the remaining regions experienced price increases in July. In the South, the median price increased 2.4% to $92,900. The Midwest experienced a comparable increase of 1.8% to $79,700, while the price in the Northeast edged up 1.2% to $143,500.

In contrast to the first half of 1991, the median price of existing homes will appreciate modestly during the second half, leaving 1991 with an overall 5.8% gain to $100,700. In 1992 and 1993, the median price will continue to rise, increasing 4.2% and 4.4%, respectively. The median price of new single-family homes is expected to fall 1.0% in 1991. By 1992, however, prices are expected to appreciate with renewed force, and the median price is projected to increase 5.2% to $127,400. Prices will continue to firm in 1993, increasing 4.3% to $132,900.

Construction

Value of Construction Put in Place

Total

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	406.9	0.1	0.3
Aug 1990	403.0	-1.0	-1.5
Sep 1990	393.3	-2.4	-4.4
Oct 1990	391.2	-0.5	-3.8
Nov 1990	388.8	-0.6	-5.6
Dec 1990	380.6	-2.1	-6.4
Jan 1991	366.5	-3.7	-11.8
Feb 1991	369.3	0.8	-12.6
Mar 1991	362.0	-2.0	-13.9
Apr 1991	364.2	0.6	-11.5
May 1991	357.2	-1.9	-12.4
Jun 1991	355.5	-0.5	-12.5
Jul 1991	***358.9***	***1.0***	***-11.8***

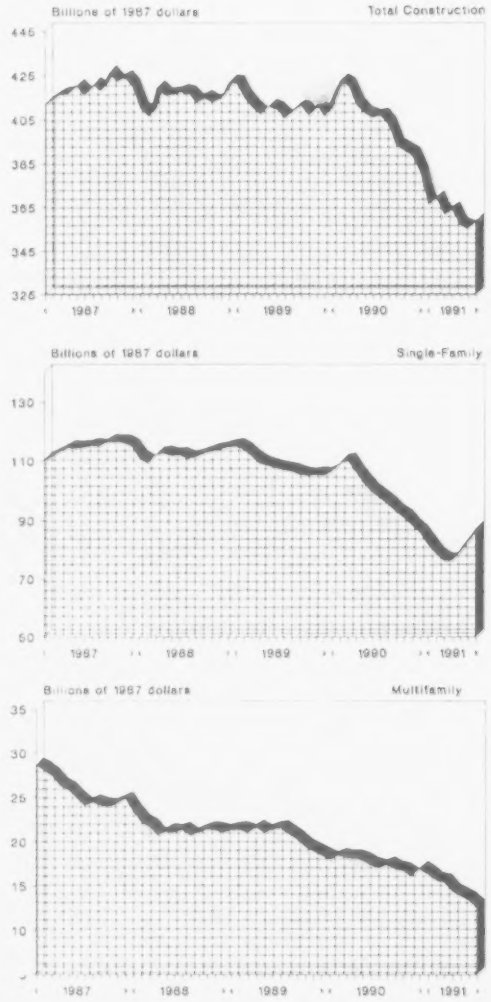
Single-Family Housing

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	97.3	-2.1	-9.0
Aug 1990	95.3	-2.1	-10.4
Sep 1990	92.8	-2.6	-11.9
Oct 1990	90.9	-2.0	-13.4
Nov 1990	88.0	-3.2	-16.4
Dec 1990	85.7	-2.6	-18.5
Jan 1991	81.8	-4.6	-23.2
Feb 1991	78.6	-3.9	-28.2
Mar 1991	76.3	-2.9	-30.6
Apr 1991	76.4	0.1	-27.9
May 1991	79.9	4.6	-21.9
Jun 1991	83.4	4.4	-16.1
Jul 1991	***87.2***	***4.6***	***-10.4***

Multifamily Housing

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	17.1	-1.2	-20.5
Aug 1990	17.4	1.8	-16.7
Sep 1990	16.9	-2.9	-16.7
Oct 1990	16.7	-1.2	-13.9
Nov 1990	16.1	-3.6	-15.3
Dec 1990	16.9	5.0	-8.6
Jan 1991	16.3	-3.6	-9.4
Feb 1991	15.6	-4.3	-15.2
Mar 1991	15.4	-1.3	-15.4
Apr 1991	14.4	-6.5	-20.9
May 1991	13.9	-3.5	-22.3
Jun 1991	13.4	-3.6	-22.5
Jul 1991	***12.5***	***-6.7***	***-26.9***

Levels are seasonally adjusted billions of 1987 dollars.
Source: Bureau of the Census



The total value of construction put in place increased 1.0% in July to $358.9 billion, ending a two-month 2.6% slide. In the year since the current slide began, total construction has fallen almost 12%.

In the residential sector, the value of single-family housing construction increased 4.6%, while the value of multifamily housing construction declined 6.7%. The 14.1% gain recorded in single-family construction during the past three months reflects the recent strength in single-family housing starts, and the 20% increase in starts since March indicates that this figure will be rising over the next several months. In spite of this recent spurt of activity, the figure remains 10.4% below its level of a year ago.

Value of Construction Put in Place

Offices

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	24.5	12.9	30.3
Aug 1990	20.5	-16.3	3.0
Sep 1990	20.3	-1.0	-1.5
Oct 1990	20.5	1.0	3.0
Nov 1990	20.2	-1.5	2.0
Dec 1990	20.7	2.5	8.9
Jan 1991	20.2	-2.4	-3.8
Feb 1991	20.9	3.5	-9.1
Mar 1991	20.7	-1.0	-7.6
Apr 1991	21.8	5.3	-0.5
May 1991	18.4	-15.6	-16.4
Jun 1991	18.7	1.6	-13.8
Jul 1991	***19.5***	***4.3***	***-20.4***

Industrial

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	26.4	0.4	-6.0
Aug 1990	25.8	-2.3	-10.4
Sep 1990	25.7	-0.4	-11.1
Oct 1990	25.0	-2.7	-11.7
Nov 1990	24.2	-3.2	-14.8
Dec 1990	24.0	-0.8	-12.7
Jan 1991	23.2	-3.3	-16.2
Feb 1991	23.3	0.4	-15.3
Mar 1991	22.0	-5.6	-19.1
Apr 1991	23.5	6.8	-11.7
May 1991	20.9	-11.1	-16.7
Jun 1991	20.0	-4.3	-24.0
Jul 1991	***20.2***	***1.0***	***-23.5***

Public

	Level	Mo. Ago % Chg.	Yr. Ago % Chg
Jul 1990	97.8	-1.0	9.5
Aug 1990	101.8	4.1	12.4
Sep 1990	96.6	-5.1	2.9
Oct 1990	99.9	3.4	11.1
Nov 1990	103.6	3.7	8.8
Dec 1990	100.0	-3.5	2.5
Jan 1991	92.5	-7.5	-6.2
Feb 1991	98.4	6.4	-1.7
Mar 1991	97.5	-0.9	-0.4
Apr 1991	96.3	-1.2	1.3
May 1991	96.1	-0.2	-1.1
Jun 1991	95.3	-0.8	-3.5
Jul 1991	***96.4***	***1.2***	***-1.4***

Levels are seasonally adjusted billions of 1987 dollars.
Source: Bureau of the Census

For the first time in over a year, office construction posted back-to-back monthly gains in July, adding 4.3% to stand at $19.5 billion. This level of construction spending is only four-fifths of its level of a year ago. Problems with the availibility of financing and the swollen supply of unleased office space will limit the gains in this category over the next year or so.

Tight finances at the federal, state, and local levels of government will keep the lid on public construction, which broke a string of four consecutive monthly declines by gaining 1.2% in July.

Robert D. Barr
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Kimberly A. Martin
Research Economist

Forecasting & Policy Analysis

Introducing the Construction Data

Notes about the series presented on pages 8 &9

This month's *Real Estate Outlook* introduces two new pages of monthly construction data that will be updated in every issue of the *Outlook*. The tables and charts show the total figure and five major components: single-family housing, multifamily housing, office buildings, industrial buildings, and public construction. The data covers the entire U.S.

This set of data is a strong indicator of how many and how quickly construction starts are translating into actual structures. Instead of measuring total contract awards or the number of housing starts, which emphasize imminent rather than current economic activity, this data measures the value of the construction that has actually been completed, or "put in place," during the month. Thus, projects which appear as housing starts in one month eventually impact construction put in place data over several months as work on the projected is completed.

Definitions

The definition of new construction used in the compilation of this data includes new buildings and structures, additions, alterations, major replacements, mechanical and electrical installations, site preparation, and installation of some types of equipment. Not included in the definition of new construction are maintenance and repairs to existing structures, cost and installation of most types of production machinery, and land acquisition.

Variables included in the computation of the value of construction put in place are the cost of materials, cost of labor and equipment, contractor's profit, cost of engineering and architectural work, overhead costs, and interest and taxes paid during construction.

While the value of improvements and additions to residential units are included in the **Total** figure presented on page 8, it is excluded from the two residential series shown on that page so that they represent construction on new housing units only.

Inflation Adjustment

The data presented on pages 8 and 9 has been adjusted for inflation. The levels are reported in terms of *1987 Dollars*, reflecting what the value of the construction would have been if prices prevalent in 1987 were in effect.

Total Construction

As Measured in Nominal and 1987 Dollars

Source: Bureau of the Census

The price adjustment provides a measure of actual, or real, economic activity. For example, if the total amount spent on housing construction in a year increases 5% from the preceding year but cost of resources used to construct these homes has increased 10%, then the actual level of economic activity has really dropped. The conclusion about the health of the construction sector may change significantly after price effects are omitted.

The importance of removing the distortion of changing prices can be seen on the chart shown on the previous page. From 1979-82, the total amount spent on construction, or the nominal value, was rising. After rising prices are factored out, we see that the price-adusted, or real, volume was falling sharply. In another case, the nominal value of construction was rising during the 1986-90 period, but the real measure shows how activity was slowly eroding. The two lines cross in 1987 since that is the base year for the inflation adjustment.

Methodology

The data for single-family structures is computed using housing starts data multiplied by an average constant cost figure and adjusted to eliminate non-construction costs. These total costs were then divided over the course of a year using fixed patterns of monthly construction progress. The fixed patterns of monthly construction progress is a table of estimates used to approximate the percentage of the project which will be completed in each month of a twelve month construction period. These percentages are then multiplied by total construction costs to determine the value of construction put in place for a given month.

For multifamily homes, the value of construction put in place is computed using cost reports collected in a survey conducted by the U.S. Department of Commerce of 2100 hundred projects in progress. Costs from this data sample were then weighted and the weights were used to derive a value for total construction put in place.

Data for the industrial and office sectors is also computed using information from a survey of a sample number of projects in progress. The responses from 5,800 projects were weighted and used in tandem with information provided by an independent research firm to determine the value of construction put in place for these sectors.

The public construction table and chart contain the value of construction put in place data for all projects financed by federal, state, or local governments. Federal project data was collected by the Census Bureau from each federal agency involved in construction activities, while state and local data was derived using a survey of about 5,800 projects.

All the data included in the tables and charts has been seasonally adjusted to help reveal underlying trends and business cycles.

Source: Bureau of the Census, Publication C30-9105: Value of Construction Put in Place, May 1991, pages 53-68.

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Jason B. Guesman
Research Assistant
Forecasting & Policy Analysis

U.S. Economic Outlook: September 1991

	91.1	91.2	91.3	91.4	92.1	92.2	92.3	92.4	1989	1990	1991	1992	1993
U.S. Economy													
Annual Growth Rate													
Real GNP	-2.8	-0.1	2.9	2.3	2.9	2.7	3.1	2.2	2.5	1.0	-0.3	2.5	2.5
Industrial Production	-9.6	2.2	6.1	4.1	3.9	4.7	5.9	4.6	2.6	1.0	-1.8	4.5	4.6
Civilian Employment	-2.4	0.3	-0.1	1.2	1.4	1.5	1.6	1.3	2.0	0.5	-0.8	1.1	1.3
GNP Inflation Index	5.2	4.2	3.3	3.2	3.3	2.6	2.6	2.6	4.1	4.1	4.0	3.1	2.8
Consumer Prices	3.5	2.1	3.1	3.4	3.4	3.2	3.4	3.5	4.8	5.4	4.3	3.3	3.4
Value of the U.S. Dollar	8.0	45.9	4.7	-0.5	-1.8	-1.3	-1.1	-0.9	6.2	-9.6	2.6	1.9	0.3
Percent													
Mfg. Capacity Utilization	78.0	77.8	78.4	79.0	79.5	80.2	81.1	81.8	84.0	82.3	78.3	80.6	83.3
Civilian Unemployment	6.5	6.8	6.8	6.7	6.7	6.6	6.5	6.4	5.3	5.5	6.7	6.6	6.3
Percent of GNP													
Federal Tax Receipts	20.4	20.3	20.2	20.3	20.5	20.5	20.5	20.5	20.2	20.3	20.3	20.5	20.5
Federal Expenditures	22.7	23.6	23.6	24.2	24.4	24.3	24.1	23.9	22.8	23.3	23.5	24.2	23.7
Federal Budget Deficit	-2.3	-3.3	-3.4	-3.9	-3.9	-3.8	-3.6	-3.4	-2.6	-3.0	-3.2	-3.7	-3.1
Interest Rates, Percent													
Federal Funds Rate	6.4	5.9	5.6	5.5	5.7	5.8	5.8	5.8	9.2	8.1	5.9	5.8	5.8
3-Month T-Bill Rate	6.0	5.6	5.4	5.3	5.3	5.2	5.2	5.1	8.1	7.5	5.6	5.2	5.1
Prime Rate	9.2	8.7	8.4	8.2	8.2	8.4	8.3	8.3	10.9	10.0	8.6	8.3	8.2
Discount Rate	6.2	5.7	5.4	5.1	5.1	5.1	5.1	5.1	6.9	7.0	5.6	5.1	5.0
Corporate AAA Bond Yield	8.9	8.9	8.7	8.5	8.4	8.3	8.2	8.0	9.3	9.3	8.8	8.2	7.6
30-Year Government Bond Yield	8.2	8.3	8.2	7.9	7.8	7.8	7.7	7.6	8.4	8.6	8.1	7.7	7.3
Mortgage Rates, Percent													
30-Year Fixed Rate	9.5	9.5	9.3	9.1	9.0	9.0	8.9	8.7	10.3	10.1	9.4	8.9	8.4
1-Year Adjustable	8.1	7.6	7.1	7.0	6.9	6.9	6.8	6.8	9.3	8.4	7.2	6.8	6.7
Home Sales & Starts													
Thousands													
Total Single-Family Sales*	3,798	4,286	4,295	4,333	4,350	4,401	4,444	4,477	4,413	4,164	4,178	4,418	4,587
Existing Single-Family Sales	3,093	3,480	3,423	3,459	3,484	3,515	3,529	3,558	3,440	3,296	3,364	3,522	3,621
New Single-Family Sales	464	506	487	511	519	534	551	564	650	534	492	542	593
Housing Starts	915	997	1,072	1,079	1,073	1,102	1,156	1,179	1,376	1,193	1,016	1,128	1,279
Single-Family Units	726	831	899	901	893	914	943	948	1,003	895	839	924	997
Multi-Family Units	189	166	173	178	180	189	213	232	373	298	177	203	282
2-4 Family Units	31	31	32	32	31	32	35	37	55	38	31	33	41
5+ Family Units	158	135	141	146	149	157	178	195	318	260	145	170	241
Mobile Homes Shipped	161	174	206	223	228	234	240	239	199	188	191	235	239
Percent change -- Year Ago													
Total Single-Family Sales	-15.2	1.3	4.1	11.7	14.6	2.7	3.5	3.3	-4.4	-5.9	-0.0	5.8	3.8
Existing Single-Family Sales	-10.2	3.5	3.8	11.0	12.6	1.0	3.1	2.9	-3.6	-4.7	2.1	4.7	2.8
New Single-Family Sales	-22.3	-6.2	-6.9	8.8	11.9	5.4	13.1	10.3	-3.3	-18.5	-7.8	10.1	9.4
Housing Starts	-36.1	-17.2	-5.2	3.6	17.2	10.5	7.8	9.3	-7.5	-13.3	-14.8	11.0	13.4
Single-Family Units	-31.8	-7.2	5.0	14.6	23.0	9.9	4.9	5.1	-7.3	-10.8	-6.2	10.1	7.8
Multi-Family Units	-48.7	-46.1	-37.0	-30.5	-4.9	13.6	23.0	30.2	-8.0	-20.1	-40.7	15.1	38.7
2-4 Family Units	-27.1	-27.7	-1.3	2.0	-0.8	0.8	9.6	15.5	-5.8	-32.1	-16.1	6.3	22.0
5+ Family Units	-51.5	-49.1	-41.7	-34.9	-5.7	16.5	26.0	33.3	-8.3	-18.0	-44.3	17.0	42.0
Median Home Prices													
Thousands of Dollars													
Existing Home Prices	95.9	101.1	102.7	103.0	103.6	104.5	105.4	106.2	93.1	95.5	100.7	104.9	109.5
New Home Prices	120.2	120.0	120.7	123.2	125.4	126.3	128.3	129.5	120.0	122.9	121.1	127.4	132.9
Percent Change - Year Ago													
Existing Home Prices	0.5	4.7	6.3	11.7	8.0	3.3	2.6	3.1	4.4	2.6	5.8	4.2	4.4
New Home Prices	-2.9	-5.2	3.5	1.0	4.3	5.2	6.2	5.1	5.9	2.4	-1.0	5.2	4.3

Quarterly figures are seasonally adjusted annual rates.

* Total single-family sales equals single-family resales plus 97% of single-family housing starts.

Source: Forecast produced using Laurence H. Meyer & Associates' model of the U.S. economy. Assumptions and simulations by Dr. John Tuccillo, Robert Barr and Kimberly Martin.

The *Real Estate Outlook* features a monthly summary of the current condition of the U.S. economy, easy-to-read forecasts for the economy and real estate, and selected reports on issues affecting the housing industry. In addition, one of the nation's top real estate economists, Dr. John Tuccillo, gives his commentary on the state of the economy and its implications for real estate markets.

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Editorial questions can be directed to Robert Barr at (202) 383-7525.

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Real Estate OUTLOOK

October 1991

With oil prices back to pre-crisis levels, sharply lower interest rates, and economic growth returning in the third quarter, the fourth quarter was supposed to see even stronger growth. But virtually all of the anecdotal evidence and a growing amount of the statistical evidence suggests a recovery that's still seriously limping. According to the NAR forecast, lower interest rates, the restocking of inventories and the improving inflation picture will allow the recovery to revive early next year after a stagnant fourth quarter. *Page 2*

Housing starts edged up another 0.6% in August to 1.065 million units. When compared with the average 4% monthly gains recorded since April of this year, August's performance appears lackluster. However, the stellar performance in the spring reflects the release of the pent-up demand resulting from the Persian Gulf War. Now that this has dissipated, recovery is expected to be gradual. *Page 4*

The rate of exising home sales deteriorated for the second consecutive month in August. After a 5-month rally, which resulted in an overall gain of 23.8%, the resale rate contracted 7.5% in July and another 2.1% in August. The resale rate currently stands at 3.25 million, which is 4.7% below the rate recorded one year ago. *Page 6*

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Commercial Real Estate Outlook	*Ruth Sergenian*	*Pages 10-11*

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Accent-u-ate the Positive, E-lim-i-nate the Negative

by John A. Tuccillo
Chief Economist and Senior Vice President
Real Estate Finance

Ben and Jerry's produces an ice cream flavor called (pun intended) Cherry Garcia. They promote it with a '60s style tie-dyed T-shirt bearing the legend, "What a long weird dip it's been." Without explaining this to non-Deadhead readers, let's adopt it to characterize the current recovery/recession (you make the call!).

We are experiencing an unusual sequence of economic events. By growth standards, this has been a mild recession. But in the process, the economy lost many jobs. The strength of the export sector through the recession has been insufficient to offset the shrinkage in financial services and the stagnation in high tech industries.

Moreover, we are cursed by the composition effect, because job growth has occurred in the Midwest and Pacific Northwest, while the economy lost jobs on both coasts. So, most *places* are experiencing recovery, but -- because those places are relatively unpopulated -- most *people* are not. The people who feel good in Oregon don't outweigh those who are feeling bad in Massachusetts.

Even now, we still see layoffs exceeding 2,000 per day, and the total for the year to date has exceeded all of 1990. The legacy is a limping recovery that few believe in. Consumption--some two-thirds of total economic activity--has been hamstrung by doubts that things are getting better. In a sense, consumers want to find out how the record will end before they'll get up to dance.

Housing is the same. Mortgage rates have fallen to levels unseen in fourteen years; the likelihood of further Fed easing suggests that they will decline even more. Yet, home sales seem immune from lower rates. In fact, there is a dichotomy in the market. First-time buyers -- those at the margin of homeownership -- have been highly responsive to the fall in rates and, in virtually all markets, business is brisk in the lower price ranges.

Trade-up buyers are less responsive to rates and much more sensitive to confidence factors. They see the ambiguities of the economy and are reluctant to take the risks of a larger mortgage debt on a more expensive house. That reluctance translates into a weaker market in the upper price ranges, and the total home sales number looks weak.

As mortgage rates continue to fall, more buyers will be drawn into the market. But this will be a marginal improvement; recovery of home sales will require strong job growth and a return of consumer confidence.

Consumer confidence is the key. We thought the recovery had arrived in February, when the end of the Gulf War raised spirits and opened wallets. Now it seems that it was all a mirage, a burst of pride and adrenaline that had little staying power. First consumer spending and later housing fell back into that twilight zone that is neither recession nor recovery.

The Administration and the Congress chose to ride that false wave of optimism, adopting a cheerleading posture that urged consumers to (in the words of the song) *"put me on the highway, and show me a sign and take it to the limit one more time"* -- i.e., recreate the spending orgy of the Eighties. This would take the place of any real and creative solution to the recession.

Unfortunately, it's not that simple. Public relations sloganeering could not hide the installment bills that arrived every month, or disguise the unemployment numbers. The American people have translated these facts into a deep pessimism about the future, made all the more painful by the high hopes of last February. Astonishingly, the result has been the first time in memory that the *public* was more pessimistic than the *economists*.

Jobs are also a problem, not only in numbers but in types. This was a "white collar" recession in that the jobs we lost were largely managerial and located in big cities. To a great extent, this explains why the recession was felt more deeply in housing and in the Northeast. Even as the economy comes back, there is little assurance that the jobs we gain will go to the same faces in the same places.

This recession has occurred amidst a changed structure of economic activity. Globalization and technological change will drive the economy of the Nineties; the recession of 1981-82 forced businesses to become leaner in the management of their resources; evolution in the financial sector has decimated the corps of middle managers; and an information based society puts a high premium on knowledge skills.

All this suggests a reshuffling of economic activity toward smaller enterprises serving a global market and located in second tier cities. These are the sectors that will ultimately produce recovery. But where does this leave economic policy? Creating the best environment for these changes involves a focus on investment incentives, education and capital renewal. In short, the signposts point to a "back to basics" economic policy.

In the short term, the economy will recover. The more relevant question, however, is: recover to what? Real growth in the Nineties requires a commitment to savings and investment on a national level. The military standdown facing us ought to provide some seed money. Ultimately, though, recovery will entail revitalization.

This month, the President attended the Country Music Association awards ceremonies. He heard there one of the best policy prescriptions any economist could offer him in the words of a song by Ricky Van Shelton:

Keep your hands on the wheel,
Believe in the things that are real.
Take your time, and keep it between the lines.

Outlook for the Economy

From the outset of the year, the fourth quarter of 1991 was expected to be everything the first quarter wasn't. At the beginning of the year, the economy was coping with a recession, a 60% runup in oil prices, and the uncertainty facing a nation on the brink of war. Now, with oil prices back to pre-crisis levels, victories recorded in both the Persian Gulf and Cold Wars, sharply lower interest rates, and a quarter of healthy economic growth under our belts, the fourth quarter is supposed to be another quarter of robust growth.

But virtually all of the anecdotal evidence and a growing amount of the statistical evidence suggests a recovery that's still seriously limping. What happened? After all, by late spring, the war was over, our oil supplies secure, and interest rates were falling. After months of pessimism and pent-up demand, the consumer was loaded for bear. The housing markets rebounded, and consumer spending rose. The recovery, while modest, seemed certain. Now it appears the consumers were, in fact, barely loaded -- income growth did not keep pace with spending, debt remained high, and the saving rate fell. All of this caught up with the consumer, and now it's the recovery that appears shot.

According to the NAR forecast, lower interest rates, the restocking of inventories and the improving inflation picture will allow the recovery to remain intact, although the fourth quarter's projected 1.3% rate of expansion will feel like the continuation of the recession to many regions and industries. The rate of growth is expected to double to 2.6% in 1992's first quarter and then reach 3.6% the following quarter. In all, the economy is expected to record a 0.5% contraction in 1991 and a 2.5% expansion in 1992.

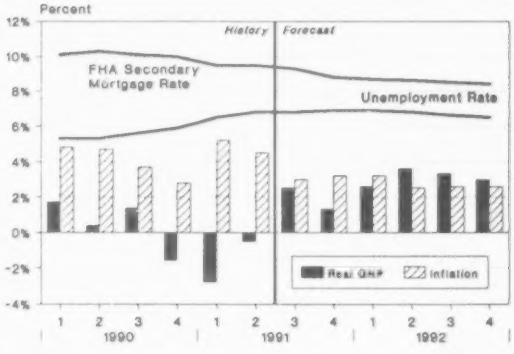
Second Quarter Momentum Spills Over

Third-quarter figures will look healthy when the initial estimates are released at the end of October. Largely reflecting the momentum the economy had at mid-year, they will not show how the economy has faltered in the past ten weeks or so. August's decline in consumer expenditures is only one sign of the slowing recovery. Also during August, for example, existing home sales slid for the second consecutive month, auto sales fell, and industrial production lowered its rate of increase. Also down, for the third consecutive month, was consumers' confidence about the health of the economy.

Consumption growth picked up in June and July but slipped in August (see chart). For the third quarter, a 3.3% annual growth rate is expected, pacing GNP to a 2.5% gain for the quarter. But just as momentum was building up in the early part of the summer, it began dropping off in late summer. While the fourth quarter is expected to see growth -- instead of a dip back into recession -- the economy's increase is expected to be just half of the previous quarter's gain.

Worsening job prospects and slow income growth have dampened consumer enthusiasm. The consumer has also been squeezed by a rising tax burden. Taxes collected from households rose at a 6.7% average annual rate since the end of 1988; personal income, the underlying source of these revenues, grew at only a 5.5% rate. The budget shortfalls that shuttered some state governments earlier

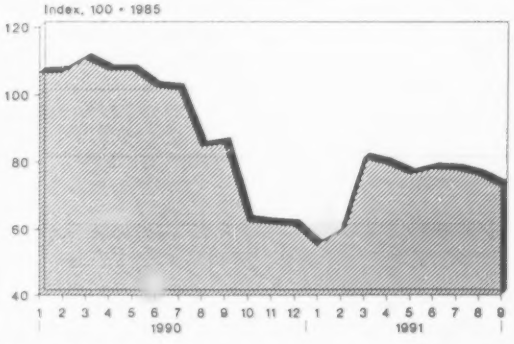
The Economic Outlook



Sources: BEA, BLS, FHLMC, NAR forecast

Consumer Confidence On the Wane

Continues Trend Seen Since Before Gulf Crisis



Source: Conference Board

Consumer Expenditure Gains Fuel Third Quarter Growth

Source: Bureau of Economic Analysis

this year came in the face of a 7.2% rate of increase in state and local personal tax receipts.

Employment Growth Returns

After two quarters of decline, nonfarm employment showed modest growth in the third quarter (see chart). Manufacturing employment, which had been particularly hard-hit in the year's first half, squeaked out a 0.3% gain. In September, the unemployment rate fell to 6.7% from the 6.8% rate recorded in the two previous months. The rate is expected to reverse course in coming months, returning to 6.8% due to the fourth quarter's slow growth. By mid-1992, the unemployment rate is expected to resume its descent, reaching 5.9% by the end of 1993. The numerous layoffs and corporate restructurings that have been announced recently will be countered somewhat by less heralded expansions in other sectors of the economy.

Fed Shows Patience

As usual, the Federal Reserve is caught in a tight spot where patience, rather than action, may turn out to be a virtue. The Fed lowered its target on the bellwether federal funds rate in August and again in September, and now it appears to be standing pat, waiting to see if these moves will be enough to revive the recovery. Overstimulating the economy by making further cuts at this point in the recovery is a trap that's caught the Fed before. The result is more inflation -- and higher long-term interest rates -- down the road. Of course, it's unclear that another interest rate cut would in fact overstimulate the economy. Given the weakness of the recovery, another rate cut or two may mean the difference between weak growth and suffering another quarter or two of contraction.

The Fed is also getting some help from long-term rates, which began falling in late July after remaining steady throughout most of the year (see chart). Yields on 30-year fixed mortgages, for example, have slipped by over a half-point since early August, and now stand close to 8.9%. Consequently, the Fed is waiting to see what effect these lower rates will have on the economy.

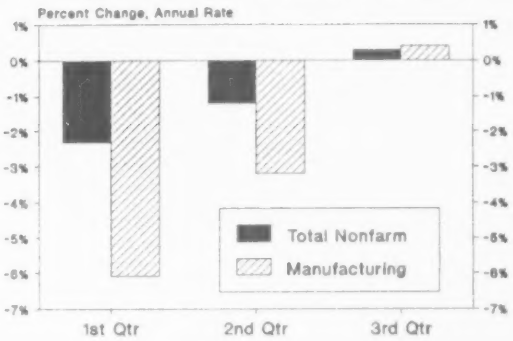
Inflation Remains A Bright Spot

The economy is expected to receive a lift from the continuing moderation of inflation, as shown in the chart. While reflecting the general weakness in the economy, lower inflation enhances consumer purchasing power and allows interest rates to fall further. In the past six months, consumer prices rose at a 2.2% annual rate, while the core index, which excludes food and energy prices, rose 3.3%. This compares with 1990's increases of 6.1% and 5.2%, respectively. Inflation at the producer level has actually disappeared in the past six months, as the Producer Price Index posted a 0.2% annual rate of decline. According to the forecast, inflation as measured by the Consumer Price Index is projected to rise only 4.2% in 1991 and 3.2% in 1992.

Robert D. Barr
Director of Forecasting
Forecasting & Policy Analysis

Employment On The Mend

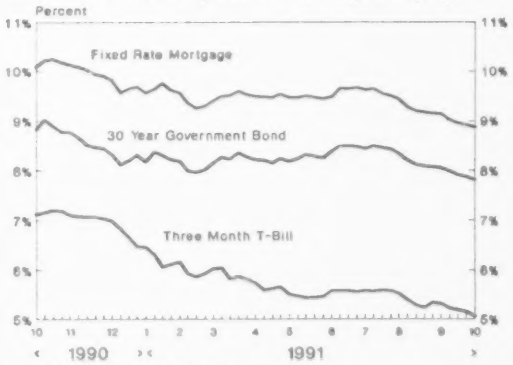
Steep Declines Over, But Recent Gains Weak



Source: Bureau of Labor Statistics

Interest Rates Slide

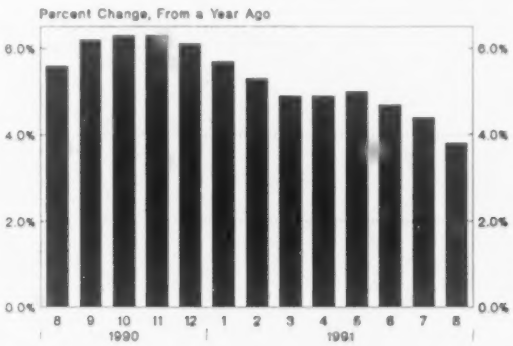
Fall for Long-Term Rates Began in July



Source: Federal Reserve Board

Inflation Moderates

Consumer Price Index



Source: Bureau of Labor Statistics